Supreme Court, U.S.
FILED

961135 JAN 2 1997

No. OFFICE OF THE CLERK

In The

Supreme Court of the United States

October Term, 1996

CITY OF DETROIT PENSION FUND and CITY OF DETROIT POLICE and FIREMAN PENSION FUND,

Petitioners,

vs.

PRUDENTIAL SECURITIES, INC.,

Respondent.

Petition for a Writ of Certiorari to the United States Court of Appeals for the Sixth Circuit

PETITION FOR A WRIT OF CERTIORARI

ROBERT N. WAGNER
Counsel of Record
WALTER L. BAUMGARDNER
MUSILLI, BAUMGARDNER, WAGNER & PARNELL, P.C.
Attorneys for Petitioners
24000 Greater Mack Avenue
St. Clair Shores, MI 48080
(810) 778-0900

70227

(800) 3 APPEAL • (800) 5 APPEAL • (800) BRIEF 21

Lutz Appellate Services, inc.

QUESTIONS PRESENTED

I. Do the District Courts have jurisdiction to interpret and determine the applicability of the National Association of Securities Dealers Code of Arbitration Procedures, which interpretation shall be final and binding upon the parties, in particular Section 15 of the National Association of Securities Dealers Code of Arbitration Procedure, prior to an arbitration hearing?

II. Do the rules of the National Association of Securities Dealers Code of Arbitration Procedure grant subject matter jurisdiction to the Federal Courts pursuant to 28 U.S.C. § 1332?

III. Does interpretation of Section 15 of the National Association of Securities Dealers Code of Arbitration Procedure grant Diversity Jurisdiction to the Federal Courts pursuant to 28 U.S.C. § 1331?

LIST OF PARTIES

The names of all parties to the proceedings in the court whose judgment is sought to be reviewed here appear in the caption of the case. Prudential Securities, Inc. is a wholly owned subsidiary of the Prudential Insurance Company.

TABLE OF CONTENTS

	Page
Questions Presented	i
List of Parties	ii
Table of Contents	iii
Table of Citations	iv
Opinions Below	1
Statement of Jurisdiction	1
Statutes Involved	1
Statement of the Case	5
Reasons for Granting the Writ	7
I. Should the courts or the Arbitrators interpret and determine the applicability of all provisions of the National Association of Securities Dealers Code of Arbitration Procedures which interpretation shall be final and binding upon the parties, in particular Section 15 of the National Association of Securities Dealers Code of Arbitration Procedure?	8
The NASD Arbitration Code of Procedure	8

Contents

Page

II. Do the rules of the National Association of Securities Dealers Code of Arbitration Procedure grant subject matter jurisdiction to the federal courts pursuant to 28 U.S.C. § 1331? 17

III. Does interpretation of Section 15 of the National Association of Securities Dealers Code of Arbitration Procedure grant diversity jurisdiction to the federal courts pursuant to 28 U.S.C. § 1332? 20

Conclusion 24

TABLE OF CITATIONS

Cases Cited:

AT&T Technologies, Inc. v. Communications Workers of America, 475 U.S. 643 (1986) 12

Brauer v. Hobbs, 151 Mich. App. 769 (1986) 14

Commodity Futures Trading Comm'n v. Schor, 478 U.S. 833 (1986) 19

Dones v. Eastern Air Lines, 408 F. Supp. 1044 (1975 D.C. PR) 21

Ford v. Hamilton Investments, Inc., 29 F.3d 255 (6th Cir. 1994) 18, 19

Contents

	Page
Gafford v. General Elec. Co., 997 F.2d 150 (6th Cir. 1993)	21
In re Prudential Sec., Inc., 795 F. Supp. 657 (S.D.N.Y. 1992)	18
In the Matter of the Application of Prudential Securities Incorporated and Prudential-Bache Properties, Inc., 795 F. Supp. 657 (S.D.N.Y. 1992)	19
Jaksich v. Thomson McKinnon Securities, Inc., 582 F. Supp. 485 (S.D.N.Y. 1984)	17
Kirkland v. E.F. Hutton & Co., 564 F. Supp. 427 (E.D. Mich. 1983)	17
Lange v. H. Hentz & Co., 418 F. Supp. 1376 (N.D. Tex. 1976)	19
Litton Financial Printing Division v. NLRB, 111 S. Ct. 2215 (1991)	12
Mastrobouno v. Shearson Lehman Hutton, 1995 U.S. Lexis 1820 at 18 Decided March 6, 1995	13, 14, 16
Miller v. E.W. Smith Co., 581 F. Supp. 817 (E.D. Pa. 1983)	17
Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc., 473 U.S. 614 (1985)	12

Contents

Page

New England Mortg. Sec. Co. v. Gay, 145 U.S. 123, 36 L. Ed. 646, 12 S. Ct. 815 21

PaineWebber, Inc. v. Farnam, 870 F.2d 507 (7th Cir. 1989) 15

PaineWebber, Inc. v. Hartmann, 21 F.2d 507 (3rd Cir. 1990) 15

PaineWebber, Inc. v. Landy, 903 F. Supp. 193 (U.S.D.C. Ma. 1995) 15

Pennsylvania Railroad Co. v. Day, 360 U.S. 548 (1959) 22, 23

Rodriguez de Quijas v. Shearson/American Express, Inc., 109 S. Ct. 1917 (1989) 11

Roney v. Kassab, 981 F.2d 894 (6th Cir. 1992) 15

Shearson/American Express, Inc. v. McMahon, 107 S. Ct. 2332 (1987) 7, 10, 14

Simon v. Smith Barney, Harris Upham & Co., (1988-1989 Transfer Binder) Fed. Sec. Law. Rep. (CCH) ¶ 94,178 at 91631 (W.D. Okla. Jan. 11, 1989) 14

United States v. Seckinger, 387 U.S. 203 (1970) 16

Washington & G.R. Co. v. District of Columbia, 146 U.S. 227, 36 L. Ed. 951, 13 S. Ct. 64 21

Contents

	Page
Watling Lerchen & Co. v. Ormand, 86 Mich. App. 238 (1978)	17
Wiepking v. Prudential Bache Securities, Inc., 940 F.2d 996 (6th Cir. 1991)	12, 14
Statutes Cited:	
9 U.S.C. § 2	1, 22
9 U.S.C. § 4	2, 11, 19
9 U.S.C. § 10	6, 16
28 U.S.C. § 1254(1)	1
28 U.S.C. § 1331	i, 1, 2, 3, 6, 17
28 U.S.C. § 1332	i, 1, 3, 6, 20
28 U.S.C. § 1332(b)	20
28 U.S.C. § 2201	20, 23
45 U.S.C. § 151, *et seq.*	22
Rule Cited:	
New York Stock Exchange Rule of Procedure 603	15

Contents

Page

Other Authorities Cited:

NASD Code of Arbitration Procedures:

§ 1 8

§ 6 8

§ 12 8

§ 15 ..... 6, 7, 8, 9, 10, 14, 15, 17, 18, 19

§ 16 ..... 8, 9

§ 21 ..... 8, 9

§ 35 ..... 6, 8, 10, 14, 15, 16, 22, 23

APPENDIX

Appendix A — Order of the United States Court of Appeals for the Sixth Circuit Filed October 4, 1996 ..... 1a

Appendix B — Judgment of the United States Court of Appeals for the Sixth Circuit Filed July 31, 1996 ..... 3a

Appendix C — Judgment of the United States District Court for the Eastern District of Michigan, Southern Division Dated January 3, 1995 ..... 5a

Petitioners, City of Detroit Pension Fund and City of Detroit Police and Fireman Pension Fund, respectfully petition for a writ of certiorari to review the judgment of the United States Court of Appeals for the Sixth Circuit.

OPINIONS BELOW

The opinion of the Court of Court of Appeals is reported at 91 F.3d 26 and is reproduced in the Supplemental Appendix. The unreported opinion of the District Court in this case is also reproduced in the Supplemental Appendix.

STATEMENT OF JURISDICTION

The Court of Appeals entered its judgment on July 31, 1996 and denied the Petition for Rehearing En Banc on October 3, 1996. The jurisdiction of this Court is invoked under 28 U.S.C. § 1254(1).

STATUTES INVOLVED

The pertinent provision of the Federal Arbitration Act, 9 U.S.C. § 2, and Sections of Title 28, Judiciary and Judicial Procedure, 28 U.S.C.A. § 1331 and 8 U.S.C.A. § 1332 are set forth below:

> United States Code Annotated
> Title 9. Arbitration
> Chapter 1— General Provisions
>
> *9 U.S.C. § 2.* Validity, Irrevocability And Enforcement Of Agreements To Arbitrate
>
> A written provision in any maritime transaction or a contract evidencing a

transaction involving commerce to settle by arbitration a controversy thereafter arising out of such contract or transaction, or the refusal to perform the whole or any part thereof, or an agreement in writing to submit to arbitration an existing controversy arising out of such a contract, transaction, or refusal, shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract.

United States Code Annotated
Title 9. Arbitration
Chapter 1 — General Provisions

9 U.S.C. § 4 A party aggrieved by the alleged failure , neglect, or refusal of another to arbitrate under a written agreement for arbitration may petition any United States District court which, save for such agreement, would have jurisdiction under Title 28, in a civil action or in admiralty of the subject matter of a suit arising out of the controversy between the parties, for an order directing that such arbitration proceed in the manner provided for in such agreement.

28 U.S.C.A. § 1331

Title 28. Judiciary And Judicial Procedure
Part IV — Jurisdiction And Venue
Chapter 85 — District Courts; Jurisdiction

§ 1331. Federal question

The district courts shall have original jurisdiction of all civil actions arising under the Constitution, laws, or treaties of the United States.

28 U.S.C.A. § 1332

Title 28. Judiciary And Judicial Procedure
Part Iv--jurisdiction And Venue
Chapter 85 — District Courts; Jurisdiction

§ 1332. Diversity Of citizenship; amount in controversy; costs

(a) The district courts shall have original jurisdiction of all civil actions where the matter in controversy exceeds the sum or value of $50,000, exclusive of interest and costs, and is between —

(1) citizens of different States;

(2) citizens of a State and citizens or subjects of a foreign state;

(3) citizens of different States and in which citizens or subjects of a foreign state are additional parties; and (4) a foreign state, defined in section 1603(a) of this title, as plaintiff and citizens of a State or of different States.

For the purposes of this section, section 1335,

and section 1441, an alien admitted to the United States for permanent residence shall be deemed a citizen of the State in which such alien is domiciled.

(b) Except when express provision therefor is otherwise made in a statute of the United States, where the plaintiff who files the case originally in the Federal courts is finally adjudged to be entitled to recover less than the sum or value of $50,000, computed without regard to any setoff or counterclaim to which the defendant may be adjudged to be entitled, and exclusive of interest and costs, the district court may deny costs to the plaintiff and, in addition, may impose costs on the plaintiff.

(c) For the purposes of this section and section 1441 of this title —

(1) a corporation shall be deemed to be a citizen of any State by which it has been incorporated and of the State where it has its principal place of business, except that in any direct action against the insurer of a policy or contract of liability insurance, whether incorporated or unincorporated, to which action the insured is not joined as a party-defendant, such insurer shall be deemed a citizen of the State of which the insured is a citizen, as

STATEMENT OF THE CASE

The original claim for arbitration was filed with the National Association of Securities Dealers (NASD) on or about February 2, 1994. The claim was served on the Respondent Prudential Securities Inc. (PSI) by the NASD on or about March 8, 1994. The claim alleged violation of various rules of the NASD, violation of fiduciary duty, violation of the Michigan Uniform Securities Act, the 1933 Securities Act and the 1934 Securities Exchange Act. The Claim for Arbitration demanded arbitration of the claims in accordance with the NASD Code of Arbitration Procedure. At the time the Claim for Arbitration was filed, Respondent Prudential Securities Inc. (PSI) was a member of the NASD. Section 1 of the NASD Code of Arbitration requires its members to arbitrate any disputes with clients The documents signed by Petitioners when they opened their account with PSI, also contained a clause which required the Defendant PSI to arbitrate any disputes between the parties. Without discussion with the attorney for Petitioners, the NASD unilaterally granted Respondents an extension of time to answer the Claim for Arbitration. Finally on April 26, 1994, Respondent PSI informed the NASD that Respondent was not going to answer the Claim, but institute litigation which is a violation section 6 of the NASD Code of Arbitration. The NASD did nothing to enforce the contract of arbitration. Respondent failed to answer the Claim for Arbitration. The NASD refused to schedule the hearing based upon letters which Defendant PSI sent to the NASD stating they were not going to answer the Demand for Arbitration. The Petitioners requested the NASD to enter the default of Respondent PSI. When the NASD refused to either schedule the arbitration or enter a default, the Funds then filed a Petition for Entry of Default with the District Court, which Respondent answered and filed its Counter Petition for Declaratory Judgement which Declaratory Judgment, the District Court granted.

The decision of the District Court was based upon Section 15 of NASD Code of Procedure, which sets the time limits for the eligibility of the submission of claims to arbitration. The District Court failed to address the duties of the Director of Arbitration for the NASD in determining eligibility of claims, specifically, Section 1 which states that the Code governs any dispute and Section 35 which states that it is for the arbitrators to interpret the NASD Arbitration Code of Procedures. The granting of the Petition for Declaratory Judgement by the District Court was based strictly on the District Court's interpretation of Section 15 of the NASD Code of Arbitration Procedure. The District Court failed to address the language of Section 35 of the NASD Code of Arbitration, which states that it is for the arbitrators to interpret the NASD Code of Procedure. Had the Court ordered the matter to arbitration, then Prudential Securities could have moved to vacate any decision pursuant to 9 U.S.C. § 10.

On appeal, the United States District Court of Appeals for the Sixth Circuit upheld the decision of the District Court. While it appears from the decision that the Sixth Circuit agrees that 28 U.S.C. § 1331 does not grant subject matter jurisdiction, the Circuit Court without discussion decided that the District Court had jurisdiction pursuant to 28 U.S.C. § 1332. Neither the District Court nor the Sixth Circuit correctly addressed the 28 U.S.C. § 1332. The Counter\complaint and Motion for Declaratory Judgment did not meet the jurisdictional amount in controversy. The courts looked at the collateral value of the of the Claim for Arbitration, which this Court has said it cannot do.

Additionally, the Circuit Court did not address Section 35 of the NASD Code of Arbitration Procedure, which states that it is for the arbitrators to interpret the Code. This Court must tell all of the District Courts and Circuit Court to let the arbitrators do their job, and only hear Petitions to Vacate pursuant to 9 U.S.C. § 10.

REASONS FOR GRANTING THE WRIT

The Court should grant the writ in order to resolve a five to five split between the federal circuit courts to determine who has the jurisdiction to interpret the eligibility of claims for arbitration pursuant to Section 15 of the National Association of Securities Dealers Code of Arbitration Procedure. Five of the circuits have ruled that it is for the arbitrators to decide, and five of the circuits have ruled that it is for the courts to decide.

Without a "definite rule" the outcome of claims for arbitration filed with the National Association of Securities Dealers, pursuant to its Code of Arbitration Procedure will be determined by the circuit in which the investor lives, not the merits of the claim. Additionally, by having the Courts determine eligibility questions, the federal courts are still in the securities fraud business, which was supposed to end with this Court's decision of *Shearson/American Express, Inc. v. McMahon,* 107 S. Ct. 2332 (1987).

Some of the Circuits, such as the Sixth, allow for a tolling of the eligibility requirements of Section 15 of the Code if fraudulent concealment has been pled with specificity. This puts the courts in the position of determining how much concealment is enough to toll the eligibility requirements. This should be decided by the arbitrators after they have heard all of the evidence.

Finally, by telling the courts to stay out of the arbitration procedure, until after the decision of the arbitrators, the court will finally enforce the arbitration contract that the securities industry prayed for when it had the decision in *Wilko v. Swan* overturned by this Court in *Shearson/American Express, Inc. v. McMahon,* 107 S. Ct. 2332(1987).

I.

DO THE DISTRICT COURTS HAVE JURISDICTION TO INTERPRET AND DETERMINE THE APPLICABILITY OF ALL PROVISIONS OF THE NATIONAL ASSOCIATION OF SECURITIES DEALERS CODE OF ARBITRATION PROCEDURES WHICH INTERPRETATION SHALL BE FINAL AND BINDING UPON THE PARTIES, IN PARTICULAR SECTION 15 OF THE NATIONAL ASSOCIATION OF SECURITIES DEALERS CODE OF ARBITRATION PROCEDURE PRIOR TO AN ARBITRATION HEARING?

THE NASD ARBITRATION CODE OF PROCEDURE

Prudential Securities Inc. (PSI) is a member of the National Association of Securities Dealers (NASD), and as a member is subject to the *NASD Code Of Arbitration Procedure.* Members of the NASD are required, at the demand of the nonmember client, arbitrate any disputes between them. Among the key provisions of the NASD Code of Arbitration which are pertinent to this appeal are sections 1, 6, 12, 15, 16, 21 and 35 which expressly provide as follows:

LEGAL PROCEEDINGS

> Sec.6. *No* party shall, during the arbitration of any matter prosecute or commence any suit, action or proceeding against any other party touching upon any of the matters referred to arbitration pursuant to this Code.

REQUIRED SUBMISSION

> Sec. 12. (a) *Any* dispute, claim or

controversy eligible for arbitration under Part I of this Code between a customer and a member and/or associated person arising in connection with the business of such member or in connection with the activities of such associated persons *shall be arbitrated under this Code,* as provided by any duly executed and enforceable written agreement or upon the demand of the customer.

ELIGIBILITY

Sec. 15. No dispute, claim, or controversy shall be eligible for submission to arbitration under this Code where six (6) years have elapsed from the occurrence or event giving rise to the act or dispute, claim, or controversy. This section shall not extend applicable statutes of limitation, nor shall it apply to any case which is directed to arbitration by a court of competent jurisdiction.

DISMISSAL OF PROCEEDINGS

Sec. 16. At any time during the course of an arbitration, the arbitrators may, either upon their own initiative or at the request of a party, dismiss the proceeding and refer the parties to the remedies provided by applicable law. The arbitrators shall at the joint request of all the parties dismiss the proceedings.

Sec. 21(b)(1) Within twenty (20)

> business days from receipt of the Statement of Claim, the Respondent(s) shall serve each party with an executed Submission Agreement and a copy of the Respondent's Answer. . . . The Answer shall specify all available defenses and relevant facts thereto that will be relied upon at the hearing. . . .
>
> INTERPRETATION OF CODE
>
> Sec. 35. The arbitrators shall be empowered to interpret and determine the applicability of all provisions under this Code which interpretation shall be final and binding upon the parties.

The Plaintiff\Appellee Prudential Securities Incorporated (PSI) claimed in paragraph 17 of the original Answer, Additional Defenses and Counterclaim: "Prudential Securities at no time agreed to arbitrate the Pension Funds claims." This is a fraudulent statement. Defendant PSI was bound to arbitrate the claims of customers pursuant to the National Association of Securities Dealers Code of Arbitration Procedure section One(l), since PSI is a member firm of the NASD. The Plaintiff\Appellee PSI then proceeded to base the Counterclaim and Motion for Declaratory Judgement on Section 15 of the Code of Procedure. PSI refused to acknowledge the existence of Section 35 of the Code. Thus, PSI is bound by the Code of Procedure to submit the issue of eligibility to the arbitrators.

The Supreme Court in *Shearson/American Express, Inc. v. McMahon,* 107 S. Ct. 2332 (1987) ruled that disputes arising under Rule 10b-5 of the Securities Exchange Act were subject to agreements to arbitrate.

The Supreme Court in *Rodriguez de Ouijas v. Shearson/ American Express, Inc.*, 109 S. Ct. 1917 (1989) held that agreements to submit to arbitration, disputes arising under the Securities Act, are enforceable under the Federal Arbitration Act.

9 U.S.C. § 4 of the Federal Arbitration Act states in pertinent part: "A party aggrieved by the alleged failure, neglect, or refusal of another to arbitrate under a written agreement for arbitration may petition any United States District court which. save for such agreement, would have jurisdiction under Title 28, in a civil action or in admiralty of the subject matter of a suit arising out of the controversy between the parties, for an order directing that such arbitration proceed in the manner provided for in such agreement."

The Claim for Arbitration as originally submitted in this matter is arbitral pursuant to the NASD Constitution. Prudential Securities, Inc. by refusing to file an answer to the Claim for Arbitration and filing the Counterclaim and Motion for Declaratory Judgement sought to achieve one of two goals.

The first goal was to void the arbitration contract.

The second goal was to have the Court selectively interpret one section of the contract of arbitration in a manner which would deprive the investor of any forum for redress of the fraud committed by Prudential Securities, Inc., one of the largest frauds ever committed on the investing public.

The first step in deciding this issues presented in this writ, is to analyze the pertinent parts of the arbitration contract. Prudential Securities provided the District Court with only selected excerpts of the contract of arbitration, the NASD Code of Arbitration Procedure. Prudential Securities in paragraph 5 of the Motion to Enjoin states that eligibility for arbitration is

for the courts and not the NASD to decide, and cites several cases. The Sixth Circuit held the duty to arbitrate is a contractual one. *Wiepking v. Prudential Bache Securities, Inc.*, 940 F. 2d 996, 998 (6th Cir. 1991). ("The starting point in arbitration disputes is to determine whether the parties agree to arbitrate <the> dispute.") (quoting, *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614, 626 (1985)). A party cannot be compelled to arbitrate claims that fall outside their agreement to arbitrate. As the Supreme Court recognized in *AT&T Technologies, Inc. v. Communications Workers of America*, 475 U.S. 643 (1986):

> . . . arbitration is a matter of contract and a party cannot be required to submit to arbitration any dispute which he has not agreed to so submit . . . This axiom recognizes the fact that arbitrators derive their authority to resolve disputes only because the parties have agreed in advance to submit such grievances to arbitration.

The Supreme Court in *Litton Financial Printing Division v. NLRB*, 111 S. Ct. 2215, 2226 (1991) stated: "Whether or not a (party) . . . is bound to arbitrate, as well as what issues it must arbitrate, is a matter to be determined by the court, and a party cannot be forced to arbitrate the arbitrability issue."

AT&T Technologies put it best by stating plainly that whether a contract creates a duty to arbitrate a particular grievance is an issue for the courts to decide.

The contract of arbitration between the parties in the instant complaint was entered into when the Appellant/Defendants (Funds) opened their investment account with Prudential Securities. The new account agreement was drafted by the

Prudential Securities. The Code of Arbitration was drafted by the National Association of Securities Dealers, Inc. of which Prudential Securities is one of the owner/members, and thus a drafter of the Code. *Mastrobouno v. Shearson Lehman Hutton,* page 18, 1995 U.S. Lexis 1820 Decided March 6, 1995.

Section one (1) of the Code of Arbitration procedure states:

> This Code of Arbitration procedure is prescribed and adopted pursuant to Article VII, Section(a)(3) of the Bylaws of the National Association of Securities Dealers, Inc., (Association) for the arbitration of *any* dispute, claim or controversy arising out of or in connection with the business of any member of the Association, with the exception of disputes involving the insurance business of any member which is also an insurance company."

(Emphasis added).

Therefore the broad language encompasses any dispute involving the sale of securities. The NASD adopted the Code of Procedure which is the contract under which the parties are to arbitrate their disputes involving the sale of securities. An example of what would be excluded, are such claims for personal injury, or any dispute which does not involve the sale of securities. Current decisions, however, have held that even sexual harassment claims in the securities industry are subject to the NASD Code of Arbitration.

The above language encompasses any dispute. This necessarily includes any dispute as to the eligibility of any claim. It is hornbook law that ambiguities in a contract are held against

the drafter. *Mastrobouno v. Shearson Lehman Hutton,* page 18, 1995 U.S. Lexis 1820 Decided March 6, 1995, *Brauer v. Hobbs,* 151 Mich. App. 769, (1986).

Prudential Securities by the Motion attempted to unilaterally exempt itself from the very contract it imposes on investors. *Wiepking v. Prudential-Bache Secs., Inc.,* 940 F.2d 996 (CA 6 1991). This Circuit went on to say that the contract of arbitration simply requires Courts to enforce privately negotiated agreements to arbitrate, like other contracts in accordance with their terms. Section 35 of the Code of Arbitration states that it is for the Arbitrators to interpret the Code of Procedure, not the Courts. The filing of the Motion to Enjoin is a violation of Section 6 of the NASD Code of Arbitration Procedure, yet the National Association of Securities Dealers has done nothing to enforce the Code. *Simon v. Smith Barney, Harris Upham & Co.,* (1988-1989 Transfer Binder) Fed. Sec. Law. Rep. (CCH) Para 94,178 at 91631 (W.D. Okla. Jan 11, 1989) (citations omitted).

Prudential Securities postured the Motion to Enjoin upon an interpretation of Section 15 of the NASD Code of Procedure that cannot stand close judicial scrutiny.

The securities industry got its wish when the Supreme Court overturned the *Wilko v. Swan* decision and ordered the enforcement of arbitration agreements. *Shearson/American Express, Inc. v. McMahon,* 107 S. Ct. 2332 (1987). Now the securities industry is trying to destroy the Code of Arbitration one section at a time, as exemplified by the brief of Prudential which focuses solely on the issue of Section 15, and not the whole contract. While the Sixth Circuit has adopted the position that it for the Courts to decide eligibility of Section 15 claims, it appears that none of the Circuits that hold to this position have addressed the issue against the requirements of Section 35.

Respondent cited with approval the *Roney v. Kassab decision of the Sixth Circuit. Roney v. Kassab,* 981 F.2d 894 (6th Cir. 1992) *Roney* was based on the assumption that Section 15 of the NASD Code of Procedure was applied in the same way as Rule 603 of the New York Stock Exchange Rules of Procedure. The *Roney* decision does not address the differences between the two sections, and it does not discuss Section 15 in conjunction with Section 35. The "occurrence or event" in Section 15 of the NASD Code of Procedure does not commence the running of eligibility requirement on the date of the purchase of the security. It is the position of the NASD, that the "occurrence or event" which gives rise to the event is to be determined on a case by case basis.

The only way to determine the "occurrence or event" which gave rise to the complaint or whether there was fraudulent concealment sufficient to extend the eligibility requirements, is for the arbitrators to hear all of the evidence. *PaineWebber, Inc. v. Landy,* 903 F. Supp 193 (U.S.D.C. Ma. 1995).

The *Roney* decision can be easily distinguished. Rule 603 of the New York Stock Exchange begins to run on the date of the transaction. *Roney v. Kassab, Id.* Additionally, the facts in the Roney case show that the broker had left the Roney firm more than six years prior to the filing of the Claim for Arbitration, which is also the same fact pattern in *PaineWebber v. Hartmann,* (21 F.2d 507 (3rd Cir. 1990) and *PaineWebber, Inc. v. Farnam,* 870 F.2d 507 (7th Cir. 1989) In the instant case, the stockbroker was still with PSI at the time the claim for arbitration was filed. Neither the *Hartmann* nor the *Farnam* decision discuss the role of the Director of Arbitration in making the initial determination of eligibility. A close reading of the *Roney* opinion indicates that it is for the Director of Arbitration to makes the initial determination of the eligibility of claims for arbitration.

PSI, in the instant case, failed to comply with the NASD Code of Procedure when it failed to respond to the Claim for Arbitration, which would have allowed the Director of Arbitration to make the initial determination as to the eligibility of arbitration of the Claim for Arbitration filed by the Petitioners.

PSI should not be allowed to disregard the common-law rule of contract interpretation that a court construe ambiguous language against the interest of the party that drafted it. *United States v. Seckinger,* 387 U.S. 203 (1970). Defendants drafted the document, the NASD Code of Procedure. *Mastrobouno v. Shearson Lehman Hutton,* page 18, 1995 U.S. Lexis 1820 Decided March 6, 1995. On page 20, the Court delivers the Coup de Gras to the position of PSI. The Court said, "Finally the respondents' reading of the clauses violates another cardinal principle of contract construction: that a document should be read to give effect to all its provisions and to render them consistent with each other." (cites omitted).

Thus this Court should read Section 15 in conjunction with Section 35 and the procedures which are set forth in the NASD Code of Procedure, and issue an opinion which leaves no doubt that the arbitrators are to interpret the NASD Code of Arbitration Procedure and reverse the decision of the Circuit Court and the District Court. The aggrieved party will still be able to file a Petition to Vacate pursuant to 9 U.S.C. § 10.

II.

DO THE RULES OF THE NATIONAL ASSOCIATION OF SECURITIES DEALERS CODE OF ARBITRATION PROCEDURE GRANT SUBJECT MATTER JURISDICTION TO THE FEDERAL COURTS PURSUANT TO 28 U.S.C. § 1331?

Prudential filed the Counter/complaint and Motion for Declaratory Judgement in reliance on Section 15 of the NASD Code of Arbitration Procedure which states:

> Sec. 15. No dispute, claim, or controversy shall be eligible for submission to arbitration under this Code where six (6) years have elapsed from the occurrence or event giving rise to the act or dispute, claim, or controversy. This section shall not extend applicable statutes of limitation, nor shall it apply to any case which is directed to arbitration by a court of competent jurisdiction.

The case law very clearly says there is no private right of action for violation of an exchange or NASD rule. *Miller v E.W. Smith Co.*, 581 F. Supp. 817 (E.D. Pa. 1983) *c.f. Kirkland v. E.F. Hutton & Co.*, 564 F. Supp 427 (E.D. Mich. 1983) *Jaksich v. Thomson McKinnon Securities, Inc.*, 582 F. Supp. 485 (S.D.N.Y. 1984); *Watling Lerchen & Co. v. Ormand,* 86 Mich. App. 238 (1978).

In a case exactly on point, in which Prudential Securities sought the same relief based on Section 15 of the NASD Code of Arbitration Procedure, as it seeks in this case, it was held that the rules of the NASD Code of Procedure, and in particular

Section 15 of the NASD Code of Arbitration Procedure do not grant the Court jurisdiction to enjoin the arbitration. *In re Prudential Sec., Inc.*, 795 F. Supp 657, 659 (S.D.N.Y. 1992).

Therefore, the District Court did not have subject matter jurisdiction to decide the issues raised by Prudential Securities in the Counter/Complaint and Motion for Preliminary Injunction, and it did not have jurisdiction to issue an order barring the arbitration.

The NASD is a private corporation, and the NASD rules are established and enforced by a private association and do not give rise to federal question jurisdiction. *In re Prudential Sec., Inc.*, 795 F. Supp 657, 659 (S.D.N.Y. 1992). *Ford v. Hamilton Investments, Inc.*, 29 F.3d 255 (6th Cir. 1994).

The Sixth Circuit Court of Appeals in regards to the Court deciding eligibility issues in a case confirming a National Association of Securities Dealers arbitration award had previously stated:

> Federal courts may hear cases under the Arbitration Act only where some independent basis for federal jurisdiction exists, and the dispositive question presented here — a question that we have raised sue sponte — is whether the district court had jurisdiction over the subject matter of the instant case.

Ford v. Hamilton Investments, 29 F.3d 255 (CA 6 1994). The court went on to say:

> Subject matter jurisdiction cannot be conferred on federal courts by consent of the parties.

Commodity Futures Trading Common v. Schor, 478 U.S. 833 (1986) It is well established that Sec. 4 of the Federal Arbitration Act, 9 U.S.C. § 4, does not constitute a grant of subject matter jurisdiction.

The court in *Ford* went on to state:

> Merely referring to a federal statute, however, does not establish federal jurisdiction if the dispute does not involve a substantial question of federal law.

As stated above, the case law clearly holds that the Code of Arbitration Procedure does not involve a federal statute. The Code of Arbitration Procedure is set of rules issued by a private corporation, not a federal act. *Lange v. H. Hentz & Co,* 418 F. Supp. 1376 (ND Tex. 1976). The rules of the NASD can be changed at any time by submitting the change to the Securities and Exchange Commission. The latest recommendation of the NASD is that Section 15 of the NASD Code be eliminated.

If as stated in the *Ford* decision, there is no federal common law of contracts, and the parties are in arbitration pursuant to a contract of arbitration, the District Court had no jurisdiction to issue an order in this matter, and the District Court order must be dismissed.

In the Matter of the Application of Prudential Securities Incorporated and Prudential-Bache Properties, Inc., 795 F. Supp. 657 (S.D.N.Y. 1992), Prudential Securities moved, which motion was granted, a remand on the grounds that the federal courts lack subject matter jurisdiction over the National Association of Securities Dealers Rules of Arbitration Procedure. Therefore, this Court must overrule the Circuit Court and the District Court and order this dispute to arbitration by clearly

stating once and for all that it is for the arbitrators to interpret the NASD Code of Arbitration Procedure.

III.

DOES INTERPRETATION OF SECTION 15 OF THE NATIONAL ASSOCIATION OF SECURITIES DEALERS CODE OF ARBITRATION PROCEDURE GRANT DIVERSITY JURISDICTION TO THE FEDERAL COURTS PURSUANT TO 28 U.S.C. § 1332?

The basis for jurisdiction in the Counter-complaint and Motion for Declaratory Judgment pled by Prudential Securities was diversity of citizenship. Prudential based the allegation of diversity jurisdiction in the Counter/Complaint on 28 U.S.C. § 1332 and 28 U.S.C. § 2201. P rudential only sought declaratory relief in the Counter/complaint, as there is no allegation of monetary damages in excess of $50,000, which is required before the Court can assume jurisdiction under 28 U.S.C. § 1332 (b). Therefore, PSI did not plead the minimum dollar amount necessary to grant the Court jurisdiction. Thus 28 U.S.C. § 1332 did not provide a basis for jurisdiction.

It is assumed for purposes of this argument, that diversity of citizenship exists, as required by 28 U.S.C. § 1332, in that this dispute is between citizens of different states. Even granting Prudential that assumption, 28 U.S.C. § 1332 does not grant the Federal Courts jurisdiction to grant an injunction to stop an arbitration of a duly authorized dispute. The second requirement of 28 U.S.C. § 1332 in order for the Federal courts to exercise diversity jurisdiction over all civil actions is that the amount in controversy exceed $50,000(recently changed to $75,000).

The Counter\complaint filed by Prudential demanded an injunction, based upon an interpretation of the National

Association of Securities Dealers Code of Arbitration Procedure. This does not embody a federal cause of action, a cause of action involving a substantial federal question, an amount in controversy over $50,000 and no other independent basis for subject matter jurisdiction exists, thus the injunction must be dismissed.

In the instant case, the amount in controversy cannot exceed $50,000. In determining the amount in controversy in a given action, the collateral effect of the judgment or other matters not directly involved in the pending suit cannot be taken in consideration. *Washington & G.R. Co. v. District of Columbia,* 146 U.S. 227, 36 L. Ed. 951, 13 S. Ct. 64; *New England Mortg. Sec. Co. v. Gay,* 145 U.S. 123, 36 L. Ed. 646, 12 S. Ct. 815. If from the nature of the case as stated in the pleadings there could not legally be a judgment in excess of the jurisdictional amount, jurisdiction cannot attach even though the damages claimed in the complaint seek a sum in excess of the jurisdictional amount. *Washington & G.R. Co. v. District of Columbia,* 146 U.S. 227, 36 L. Ed. 951, 13 S. Ct. 64; *New England Mortg. Sec. Co. v. Gay,* 145 U.S. 123, 36 L. Ed. 646, 12 S. Ct. 815. The issue for the District Court to decide on the Motion for Declaratory judgment was only the interpretation of Section 15, this did not exceed the jurisdiction amount as required. The interpretation of Section 15 of the NASD Code of Arbitration does not amount to a judgment in excess of $50,000. The fact that ultimately the arbitrators might grant an award in excess of $50,000 does satisfy the jurisdictional amount as this is clearly a collateral event. Even if the Court accepts the argument that there is diversity of citizenship, there is still no private right of action for an alleged preemptory breach of the NASD Code of Arbitration Procedure. *Gafford v. General Elec. Co* , 997 F.2d 150 (6th Cir. 1993).

In a case analogous in many ways to the instant case, *Dones v. Eastern Air Lines,* 408 F. Supp. 1044 (1975 D.C. PR) the

court examined the issue of whether diversity of citizenship grants jurisdiction if the court lacks subject matter jurisdiction. The court quoted from *Pennsylvania Railroad Co. v. Day,* 360 U.S. 548 (1959) a case in which jurisdiction was based on diversity of citizenship and which the Supreme Court remanded to the District Court with instructions to dismiss for lack of jurisdiction, the disputes between the employers and employees subject to the Railway Labor Act, Title 45 United State Code Section 151 *et seq.*, must be settled by the administrative boards therein established since these boards have exclusive primary jurisdiction over said disputes.

While the Dones case was decided in relation to airline administrative boards, there is little doubt in the instant case, that the NASD arbitration panels have primary jurisdiction to decide disputes between investors and brokerage firms through the arbitration process.

9 U.S.C. § 2 states:

> A written provision in any maritime transaction or a contract evidencing a transaction involving commerce to settle by arbitration a controversy thereafter arising out of such contract or transaction, or the refusal to perform the whole or any part thereof, or an agreement in writing to submit to arbitration an existing controversy arising out of such a contract, transaction, or refusal, shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract.

In the instant case, Sec. 35 of the NASD Code of Arbitration Procedure states:

> The arbitrators shall be empowered to interpret and determine the applicability of all provisions under this Code which interpretation shall be final and binding upon the parties.

Section 35 leaves no doubt that it is for the arbitrators to interpret the Code, not the Courts. In fact, once the Claim for Arbitration is filed, the parties are barred from resorting to the Courts.

> Sec.6. *No* party shall, during the arbitration of any matter prosecute or commence any suit, action or proceeding against any other party touching upon any of the matters referred to arbitration pursuant to this Code.

Ultimately the court in *Pennsylvania Railroad* said, "Consequently the Court is of the opinion that under the terms of the Railway Labor Act, it lacks jurisdiction over the subject matter and cannot entertain the action even though diversity jurisdiction has been invoked and conceded." The same should be said of the Federal Arbitration Act and the NASD Code of Arbitration Procedure.

Therefore, the injunction must be dissolved and the parties ordered to arbitration.

28 U.S.C. § 2201 does not provide for an independent basis of jurisdiction, it only provides a remedy.

Thus, the District Court had no jurisdiction to entertain the Counter/Complaint and Motion of Plaintiff/Appellee and this Court should rule once and for all that it is for the arbitrators to hear all of the evidence and decide the issues.

CONCLUSION

For the reasons stated, the petition for a writ of certiorari should be granted.

Respectfully submitted,

ROBERT N. WAGNER
Counsel of Record
WALTER L. BAUMGARDNER
MUSILLI, BAUMGARDNER,
WAGNER & PARNELL, P.C.
Attorneys for Petitioners
24000 Greater Mack Avenue
St. Clair Shores, MI 48080
(810) 778-0900

APPENDIX A — ORDER OF THE UNITED STATES COURT OF APPEALS FOR THE SIXTH CIRCUIT FILED OCTOBER 4, 1996

No. 95-1078

UNITED STATES COURT OF APPEALS
FOR THE SIXTH CIRCUIT

CITY OF DETROIT PENSION FUND, ET AL.,

Plaintiffs-Appellants,

v.

PRUDENTIAL SECURITIES, INCORPORATED,

Defendant-Appellee.

ORDER

BEFORE: NORRIS and SUHRHEINRICH, Circuit Judges; and WELLS,* District Judge.

The court having received a petition for rehearing en banc, and the petition having been circulated not only to the original panel members but also to all other active judges of this court, and no judge of this court having requested a vote on the suggestion for rehearing en banc, the petition for rehearing has been referred to the original panel.

---

* Hon. Lesley Brooks Wells, United States District Judge for the Northern District of Ohio, sitting by designation.

Appendix A

The panel has further reviewed the petition for rehearing and concludes that the issues raised in the petition were fully considered upon the original submission and decision of the case. Accordingly, the petition is denied.

ENTERED BY ORDER THE COURT

s/ Leonard Green
Leonard Green, Clerk

APPENDIX B — JUDGMENT OF THE UNITED STATES COURT OF APPEALS FOR THE SIXTH CIRCUIT FILED JULY 31, 1996

UNITED STATES COURT OF APPEALS FOR THE SIXTH CIRCUIT

No. 95-1078

CITY OF DETROIT PENSION FUND; CITY OF DETROIT POLICE AND FIREMAN PENSION FUND,

Plaintiffs-Appellants,

v.

PRUDENTIAL SECURITIES, INCORPORATED,

Defendant-Appellee.

Before: **Norris** and **Suhrheinrich,** Circuit Judges; **Wells,** District Judge.

JUDGMENT

ON APPEAL from the United States District Court for the Eastern District of Michigan at Detroit.

THIS CAUSE was heard on the record from the district court and was argued by counsel.

IN CONSIDERATION WHEREOF, it is ORDERED that the judgment of the district court is AFFIRMED.

Appendix B

ENTERED BY ORDER THE COURT

s/ Leonard Green
Leonard Green, Clerk

A True Copy.

Attest:

Deputy Clerk

APPENDIX C — JUDGMENT OF THE UNITED STATES DISTRICT COURT FOR THE EASTERN DISTRICT OF MICHIGAN, SOUTHERN DIVISION DATED JANUARY 3, 1995

UNITED STATES DISTRICT COURT
EASTERN DISTRICT OF MICHIGAN
SOUTHERN DIVISION

Civil Action
No. 94-CV-71767-DT

HON. BERNARD A. FRIEDMAN

CITY OF DETROIT PENSION FUND; et al.,

Plaintiffs,

v.

PRUDENTIAL SECURITIES, INC.,

Defendant.

JUDGMENT

The court has granted Defendant's motion to enjoin and dismiss arbitration claim and to dismiss petition for confirmation of award. Accordingly,

IT IS ORDERED AND ADJUDGED that judgment be and is hereby granted for Defendant and against Plaintiffs.

Dated at Detroit, Michigan, JAN 3, 1995.

Appendix C

JOHN P. MAYER
CLERK OF THE COURT

By s/ J.N. Bardsai
Deputy Clerk

Approved:

s/ Bernard A. Friedman
BERNARD A. FRIEDMAN
UNITED STATES DISTRICT JUDGE